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IN THE

Supreme Court of the United States

OCTOBER TERM 1940.

NO. 564

MASCOT STOVE COMPANY, a Corporation, *Petitioner*,

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, *Respondent*.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT, AND BRIEF IN SUPPORT THEREOF.

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To the Honorable Harlan Fiske Stone, Chief Justice of the United States, and to the Associate Justices of the Supreme Court of the United States:

The undersigned, on behalf of the above named petitioner, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Sixth Circuit entered June 3, 1941, in the above entitled proceedings, docketed therein as No. 8595.

Opinions.

The opinion of the United States Board of Tax Appeals is reported at pages 27 *et seq.* of the record. The opinion of the United States Circuit Court of Appeals for the Sixth Circuit is not yet reported, but found at pages 46 *et seq.* of the record herein.

Jurisdiction.

The judgment of the United States Circuit Court of Appeals for the Sixth Circuit was entered on June 3, 1941. The jurisdiction of this Court is invoked under the provisions of Section 347(a), Title 28, U. S. C. A.

Questions Presented.

The question presented in this case is whether or not the petitioner is a corporation resulting from a reorganization within the meaning of Sections 112(i) and 113(7) of the Revenue Act of 1932, c. 209, 47 Stat. 169; also whether the decision of the Court in this case is in conflict with the decision of Courts of equal jurisdiction in other Circuits.

Statutes Involved.

Subsection (i) of Section 112 of the Revenue Act of 1932, c. 209, 47 Stat. 169, reads as follows:

> "(i) DEFINITION OF REORGANIZATION.—As used in this section and sections 113 and 115—
>
> (1) The term 'reorganization' means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation), or (B) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred, or (C) a recapitali-

zation, or (D) a mere change in identity, form, or place of organization, however effected.

(2) The term 'a party to a reorganization' includes a corporation resulting from a reorganization and includes both corporations in the case of an acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation.

(j) DEFINITION OF CONTROL.—As used in this section the term 'control' means the ownership of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of the corporation."

* * * *

Subsection (7) of Section 113 of the Revenue Act of 1932 reads as follows:

"(7) TRANSFERS TO CORPORATION WHERE CONTROL OF PROPERTY REMAINS IN SAME PERSONS.—If the property was acquired after December 31, 1917, by a corporation in connection with a reorganization, and immediately after the transfer an interest or control in such property of 50 per centum or more remained in the same persons or any of them, then the basis shall be the same as it would be in the hands of the transferor, increased in the amount of gain or decreased in the amount of loss recognized to the transferor upon such transfer under the law applicable to the year in which the transfer was made. This paragraph shall not apply if the property acquired consists of stock or securities in a corporation a party to the reorganization, unless acquired by the issuance of stock or securities of the transferee as the consideration in whole or in part for the transfer."

Statement.

The petitioner is a manufacturing corporation, organized under the laws of Tennessee, and is engaged in the business of manufacturing and selling cooking and heating stoves with its principal place of business at Chattanooga,

Tennessee, and is the successor to a prior corporation that was adjudged a bankrupt on June 20, 1933 (R. p. 27). The fiscal year involved ended June 30, 1934.

The prior corporation held a charter issued by the State of Tennessee under the name of Mascot Stove Manufacturing Company, and at the time of adjudication in bankruptcy its officers and stockholders formed themselves into a committee to be represented by Alvin Ziegler (one of such officers and stockholders) as Trustee, for the purpose of effecting a reorganization of the bankrupt corporation (R. pp. 31-32).

The old company owned unencumbered assets of the book value of $39,496.00, consisting of current inventories and accounts receivable (R. p. 32), and owned real estate, buildings, machinery, plant fixtures and good will which were encumbered by a first mortgage or deed of trust in the amount of $33,000 (R. p. 31).

The inventoried assets of the old company of the fair value of $28,184.34 in a going business (cost or market whichever is lower), was appraised in the bankruptcy proceeding at the value of $9,280.50 (R. p. 27) separate and apart from the factory building, patterns, machinery (used in their fabrication) and good will; and the current accounts receivable of $22,608.92 (subject to an assignment of $11,297.26 to a finance company) were appraised at $2,351.75 (R. p. 27).

The officers and stockholders of the old company were greatly concerned in holding together in one business unit the assets of the old company, and by negotiations through Alvin Ziegler, as their Trustee, made an agreement with the holder of the trust note of $33,000 to acquire the equity in the property pledged as security for its payment; and in pursuance of such an agreement the Trustee in Bankruptcy, representing the old company, was directed by the referee in bankruptcy to make a quit-claim deed for such mortgaged property to Luke O. Morin (as associate of Alvin Ziegler and President of the old company) as Trustee for himself and a corporation to be organized (R. p. 27).

Also, Alvin Ziegler, as Trustee for the officers and stockholders of the old company, submitted a written offer to the Trustee in Bankruptcy, as representative of the old company and its creditors, to pay to him for distribution to creditors the sum of $7,500 in cash and notes for the inventoried assets and accounts receivable of the old company (R. p. 27). It was made known by Ziegler, as Trustee for stockholders, to the Trustee of the estate of the bankrupt corporation, that it was his purpose to organize a new corporation to take over the properties, good will, and business of the bankrupt corporation; execute a new mortgage or deed of trust to the secured creditor of the bankrupt corporation, and issue the stock of the new corporation to the stockholders of the old corporation who held not less than 76 per cent of the stock of the old corporation (R. pp. 28 and 32).

Upon the payment of Ziegler, Trustee, of $2,500 to the Trustee of the estate of the bankrupt corporation, the referee in bankruptcy approved the acceptance of the offer of Ziegler as Trustee for the officers and stockholders of the old company and directed the Trustee of the bankrupt estate to turn over to Ziegler the assets and property of the bankrupt corporation; and to accept the notes of Alvin Ziegler, Trustee, for the amount of $5,000, secured by an hypothecation of the notes of the new company to be organized by Ziegler and the stockholders of the old company in the aggregate amount of $5,000 (R. pp. 31 and 34). The amount of $7,500 apparently included substantially all of the unsecured indebtedness of the bankrupt corporation that it was unable to pay promptly.

The offer of Ziegler, Trustee, was accepted by the Trustee of the bankrupt estate on July 7, 1933, and on July 8, 1933, Alvin Ziegler, Trustee, acting for the stockholders of the old company, procured a charter for petitioner, and completed its organization on July 14, 1933, by a transfer of the properties of the bankrupt estate released to him by the Trustee in Bankruptcy for that purpose (R. p. 29).

The common stock of the new company (after the payment in of $6,000 of preferred stock by common stockholders of the old company) was issued to Alvin Ziegler, Trustee, to be distributed to the stockholders of the old company in substantially the same proportion in which they held the stock of the old company at time of adjudication (R. pp. 28 and 32); and the notes of the new company in the amount of $5,000 were delivered to the Trustee in Bankruptcy.

The involuntary adjudication in bankruptcy of the Mascot Stove Manufacturing Company was not planned as a step "in pursuance of a plan of reorganization", but after the adjudication was made on June 20, 1933, it became the basis of a plan (in cooperation with the Trustee in Bankruptcy), to have the properties of the old corporation transferred to Alvin Ziegler, as Trustee for the stockholders of the old company in order that the business of the old company could be reorganized and continued without substantial interruption by keeping its properties and good will unified in the business for the benefit of *creditors* and *stockholders* (R. pp. 31-32).

There was a substantial equitable value attached to the inventoried assets of the old company and its accounts receivable, which would be lost to its creditors and stockholders in the event a reorganization of its business could not be brought about under the plan pursued; and in pursuance of the plan, the new corporation was to execute notes for unsecured debts to be delivered to the Trustee in Bankruptcy by Alvin Ziegler, Trustee (R. pp. 31 and 34).

During the period of reorganization (which began at the time of adjudication (R. p. 31), the Trustee in Bankruptcy (being in charge of the bankrupt's estate) made the transfer of its properties to the new company, or Alvin Ziegler, as Trustee for stockholders of the old company, and accepted cash and notes therefor. The cash and notes received by Ziegler from the new company were paid over to the Trustee in Bankruptcy; and the stock of the new company was delivered to the stockholders of the old company (R. pp. 31 to 34). Immediately after the Trustee of the

bankrupt transferred the properties of the old company to the new company (in pursuance of the plan of reorganization), 80 per cent or more control of the property remained in the same persons, or 76 per cent of them, who were stockholders of the old company prior to the adjudication; and during the time required to perfect the plan for a reorganization of the business of the bankrupt, no independent or adverse interest in the property was present (see findings of fact by the Board, R. pp. 27 *et seq.*). The Trustee of the bankrupt's estate acted in a fiduciary capacity; and his interest in the properties of the bankrupt was not adverse to the interest of creditors and stockholders of the old company, under the plan of reorganization that was carried out.

Notwithstanding the Board of Tax Appeals finds that there was a plan adopted for the reorganization of the business of the old company (R. p. 22), and that the plan was carried out in a way that was satisfactory to the Bankruptcy Court; and notwithstanding the Board finds that the plan provided that the stockholders of the old company should be the sole stockholders of the new company (R. p. 18), the Court of Appeals for the Sixth Circuit holds that the intervention of a bankruptcy proceeding as a part of a plan of reorganization deprives the transaction of the features of a reorganization as defined by Sections 112(i) and 113(7) of the Revenue Act of 1932. The Court holds that the new company is not entitled to the same basis of the properties acquired that was recognized for them in the hands of the old company, notwithstanding 50 per cent or more control of the properties remained in the same persons or some of them.

Specification of Errors.

The United States Circuit Court of Appeals erred:

1. In holding that officers and stockholders of a corporation that has been adjudged a bankrupt may not, with the full cooperation of the Trustee in Bankruptcy

(whose conduct is approved by the Court) effect a reorganization of its business and property within the meaning of Sections 112(i) and 113(7) of the Revenue Act of 1932, and

2. In holding that petitioner is not entitled to the same basis for the properties acquired that was recognized as the basis in the hands of the prior corporate owner, as provided by Section 113(7) of the Revenue Act of 1932.

Reasons for Granting the Writ.

1. There is a direct conflict between the decision of the Court in this case and the decision of the Court of Appeals for the Seventh Circuit in the case of *Rex Manufacturing Company* v. *Commissioner,* 102 Fed. (2d) 325; and the Court says that insofar as its decision herein is inconsistent with the decision in the case of *Rex Manufacturing Company, supra,* it declines to follow that case.

2. The question of law presented in this proceeding is identical with the question presented in the case of *Rex Manufacturing Company* v. *Commissioner,* 102 Fed. (2d) 325; and the facts in each case are not to be distinguished on the application of such question of law, and the construction of the identical statutes involved in each case (Sections 112(i) and 113(7) of the Revenue Act of 1932).

3. Also, the opinion of the Court in this case is directly in conflict with its opinion in the case of *Commissioner* v. *Newberry Lumber & Chemical Company,* 94 Fed. (2d) 447, and the opinion of the Circuit Court of Appeals for the Seventh Circuit in the case of *Commissioner* v. *Kitselman,* 89 Fed. (2d) 458. In each of the foregoing cases it was held that a reorganization within the meaning of Sections 112(i) and 113(7) of the Revenue Act of 1932 may be effected in connection with an insolvency proceeding in equity or bankruptcy.

4. In a recent opinion of the Circuit Court of Appeals for the Ninth Circuit in the case of *Commissioner* v. *Marlborough Investment Company, et al.*, decided March 8, 1941, the Court declined to follow the opinions of the Sixth and Seventh Circuits in the cases of *Kitselman* and *Newberry Lumber & Chemical Company, supra.* It is understood that an application for certiorari has been applied for in the *Marlborough Investment Company case* for a review by this Court of the decision therein; and that the Department of Justice has joined in the request for the issuance of a writ in that case.

5. It is submitted that if the writ in the *Marlborough Investment Company case, supra,* be granted to reconcile the conflict there admitted to be present by analogy; that a writ should also be granted in this case to reconcile the conflict which the Court below recognizes to be present with the case of *Rex Manufacturing Company, supra.* The opinion of the Court in the *Rex Manufacturing Company case, supra,* is based upon the opinions of the Court in the *Kitselman* and *Newberry Lumber & Chemical Company cases, supra;* and the Court of Appeals for the Ninth Circuit undertakes to depart from the decisions in the *Kitselman, Newberry Lumber & Chemical Company,* and *Rex Manufacturing Company cases, supra,* because it says those cases are in conflict with the case of *LeTulle* v. *Scofield, Collector,* 308 U. S. 415.

6. By the conflict which arises in this case, and the other cases involving related questions of law, the application of Sections 112(i) and 113(7) of the Revenue Act of 1932 (as they may be invoked under varying circumstances of fact) is in a state of hopeless confusion. Such a state of hopeless confusion in the application of Sections 112(i) and 113(7) of the Revenue Act of

1932, will prevail in the Courts below until authoritatively settled by an opinion by this Court in each case in which there is now a direct conflict.

WHEREFORE, in order to have the conflict appearing herein settled by an authoritative decision of this Court, petitioner respectfully prays that a writ of certiorari may be issued herein directed to the United States Circuit Court of Appeals for the Sixth Circuit commanding said Court to certify and send to this Court on a day certain to be therein designated a full and complete transcript of the record and proceedings of said Circuit Court of Appeals in this case, entitled *Mascot Stove Company* v. *Commissioner of Internal Revenue,* No. 8595, to the end that said case may be reviewed and determined by this Court as provided by law, and that petitioner may have such other and further relief or remedy in the premises as to this Court may seem appropriate, and that said judgment of said Circuit Court of Appeals may be reversed by this Honorable Court.

Respectfully submitted,

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